The Great Atlantic & Pacific Tea Company, Inc. Annual Report 1978

One of the most significant developments of the year was a substantial investment in A&P by a major West German food retailer. The Tengelmann Group, which has been in the food retailing business since 1893 and which operates approximately 2,000 supermarkets and limited-line discount stores in Europe, purchased 7,291,170 shares of the Company's common stock and acquired options to purchase 3,124,787 shares at any time through January 21, 1980.

This welcome expression of confidence in the future of A&P gives the Tengelmann Group approximately 29 percent of the outstanding shares of the Company, with options covering an additional 13 percent.

Tengelmann, one of the most successful European food retailing organizations, has an excellent track record of growth and profitability and has pledged to take an active and enthusiastic "partner-investor" role in our collective efforts to restore A&P to sustained profitability.

As reported at our last annual meeting, we have worked closely with an outside consulting firm, McKinsey and Company, in analyzing the potential for sales and profits in all our stores and manufacturing plants. The findings of this study led us to implement a broadscale restructuring program which will improve future Company operating results.

A net reserve of $40 million to cover the costs of this restructuring program was provided in the fourth quarter of fiscal 1978. Our operating performance during 1978 showed mixed results. Sales increased slightly from $7,288,577,000 the year before to $7,469,659,000, a gain of 2.5 percent. Average weekly sales per store continued their encouraging trend, rising from $74,741 to $81,165 or an 8.6 percent increase. Despite a return to operating profitability in the last two quarters, losses in the first two quarters caused an earnings downturn for the year ended February 24, 1979. Including the above-mentioned $40 million provision, we had a loss of $52,186,000 or $2.10 per share, compared with earnings of $569,000 or $.02 per share the year before.

As part of the restructuring program, we withdrew from the Cleveland, Milwaukee, and Pittsburgh markets, areas where we have been deeply in the red for more than 15 years. We were simply unable to turn these unprofitable units around without a major investment of capital which we believe could be better utilized elsewhere. These units and some stores that we closed in our Chicago and New England markets accounted for approximately 10 percent of the Company's sales.

Additionally, we streamlined our manufacturing operations by phasing out the Altoona, Pennsylvania bakery and the Terre Haute, Indiana food manufacturing plant; both facilities were approximately 50 years old.

This year, our goal is to sustain and improve on the earnings trend, and as always to offer quality products, friendly service, and competitive prices to our customers.

The effects of inflation on our customers, your Company and business continue to be a primary concern of your management.

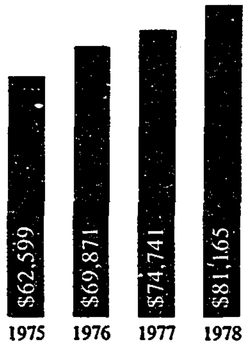
It is our belief that the food distribution industry in general, with A&P a leading participant, has long performed essential functions for the American public efficiently and at minimum cost. We are basically a pass-through industry, and thus our opportunities to control inflation are limited. Nevertheless, we accept the responsibility of doing everything we possibly can to lessen the burden of inflation for our customers.

To become more aggressive in this regard, we have introduced marketing programs such as: "Economy Corner," Action Prices, and trading stamps.

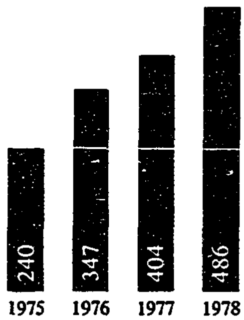
The new "Economy Corner" section in most of our stores features unbranded food and general merchandise products. Priced as much as 30 percent below national brands, these so-called

Jonathan L. Scott, Chairman of The Board of Directors and Chief Executive Officer, (left) and David W. Morrow, President and Chief Operating Officer.

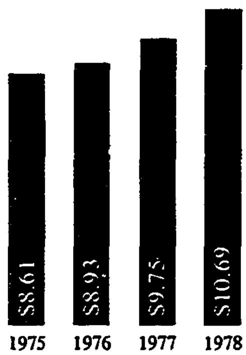
Average Weekly Sales Per Store (4th Quarter)



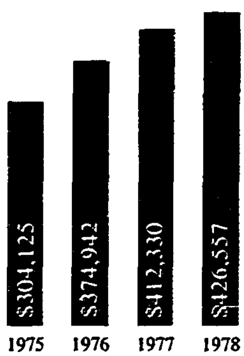
Number of Stores Over $100,000 Per Week Per Store (4th Quarter)



Average Sales Per Transaction (4th Quarter)



General Merchandise Sales (Dollars in thousands)



generic products are popular items and offer economy-minded consumers an alternative to national brands or private label products. We now offer 50 such generic products in plain black and white containers and are expanding the line in response to customer demand.

Our Action Prices Program, another successful inflation-fighting effort, passes manufacturers' allowances along to shoppers in the form of reduced prices.

Trading stamps introduced by us last year in areas where there appeared to be renewed interest in this method of getting a little something extra for the food dollar, won firm support in our Chicago, Indianapolis, and Louisville Divisions. In areas where they were not as successful, we discontinued them.

Our new advertising theme—"You'll Do Better At A&P"—enables us to reach out to our customers with a new and flexible approach designed to focus attention on specific market opportunities and our improved in-store merchandising, particularly in the produce and meat departments.

In continuing our efforts to improve earnings, this year we will build 27 supermarkets and combo-stores and enlarge or remodel 47 existing units. Also, we will increase our commitment to the limited-assortment store. Tengelmann has been extremely successful in this type store, and their experience with these stores should be very helpful to us. We intend to open a substantial number of them this year, and we believe this type store could be an excellent alternate use for many of our smaller A&P stores.

In this regard, capital spending this year will total $80,000,000. Last year, our capital expenditures were $84,273,000. We built 52 stores and enlarged or remodeled 26 stores. We closed 186 units in addition to the 174 stores closed as part of our restructuring program.

The challenge of the future, as we go forward in modernizing and expanding our total store network, without losing sight of sustained profitability, is to continue building upon a reputation begun over 120 years ago of being a dependable provider of food for the family, and above all, to please our customers.

Our financial condition remains strong. Our cash and short-term investments at year-end totaled $94,716,000, up from $26,537,000 the year before. We have had no short-term debt for over nine months, and our long-term debt decreased by $1,624,000 during the year. We have many strengths—the people, the financial resources, and the capability of pleasing our customers and giving them the most value for their money.

We wish to express our gratitude for the patronage of our customers, the loyalty of our employees, the service of our suppliers, and the support of our stockholders, all of which are so vital to the success of our Company.

Finally, we would like to pay special tribute to Forwood C. Wiser Jr. and Edwin D. Dodd who left our Board during the year and to Charles F. Detmar, Jr., William M. Agee, Edward J. Toner, and Oscar L. Dunn, Jr. who are not running for re-election. We are deeply grateful for the help, encouragement and counsel they have provided the Company during these critical years of redevelopment.

David W Morrow

David W. Morrow
President and Chief Operating Officer

J. L. Scott

Jonathan L. Scott
Chairman of The Board of Directors
and Chief Executive Officer
May 11, 1979

Success in the retail trade is dependent on the positive interaction of people. Nowhere is this truth more evident than in the supermarket business.

That is why we at A&P continue to direct so much time, energy and money toward refining the skills and improving the performance of our greatest asset—human resources.

In a company as large as ours, with some 72,000 employees located throughout the country, this undertaking involves the development of people within A&P as well as the cultivation of outside sources to locate and attract new employees. Our objective is the blending of experienced, skilled A&P people with the best that these sources have to offer.

Helping us identify talented individuals inside A&P is our Human Resource Information System (HRIS), a computerized employee data bank. This growing storehouse of information, used in combination with regular performance reviews, aids us in

pinpointing employees who show an aptitude and desire to build professional and management careers with our Company.

On completion, HRIS will be administered through five Human Resource Information Centers in the United States and Canada, making it one of the few multi-site human resource data banks in North America. The end product is a common system, custom tailored to the specific needs of the various geographic locations, with information accessible company-wide.

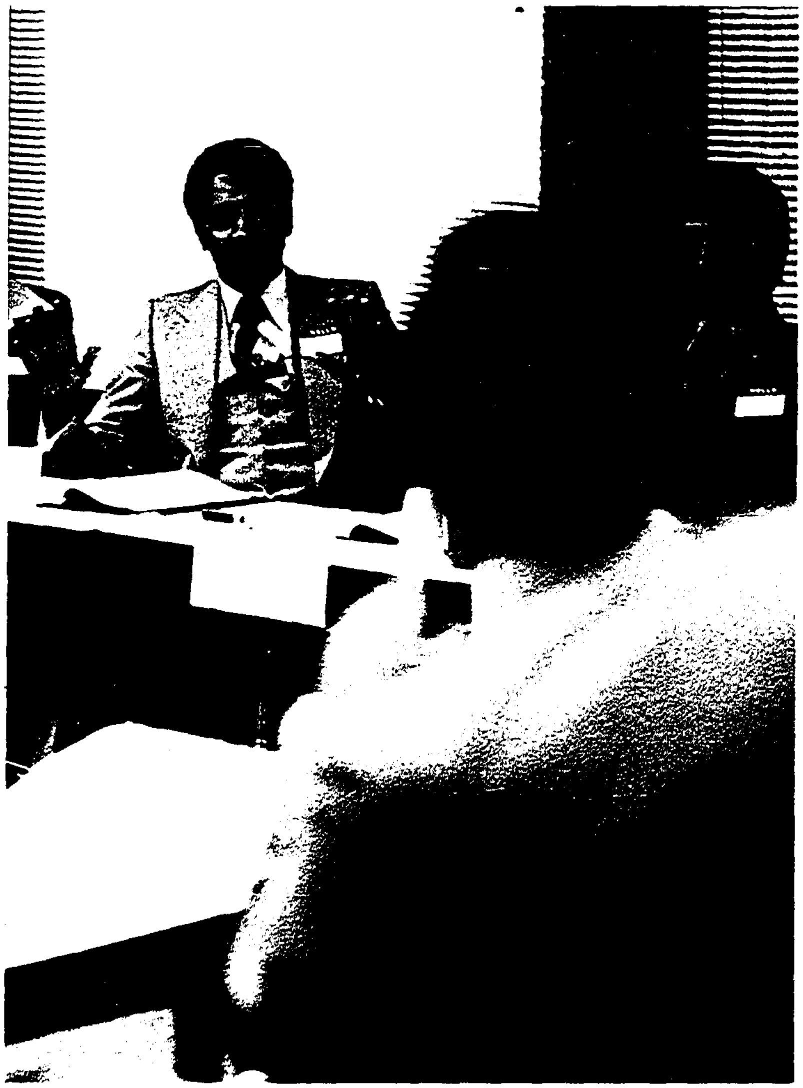
The combination of on-the-job performance tracking and the HRIS is proving effective in working with a largely untapped resource—our part-time in-store work force—to identify employees who are concurrently pursuing advanced education and are therefore prime potential candidates for management and professional career paths upon completion of their academic programs. Possessed of solid retail experience, knowledge of A&P's systems, and the motivation to combine work and study, such individuals are potentially valuable assets to A&P.

Left top: John Barone (left), who completed college while working part time at A&P, is studying to be a store manager as a candidate from our Internal Recruitment Program.

Left bottom: John's training includes Cornell University's home study course.

Center: Reviewing A&P college relations materials at Cornell University's Department of Agricultural Economics are, from left, George V. Malone, director of A&P corporate recruitment; Olan D. Forker, department chairman; Mary M. Cagney, A&P staffing manager; and Gene A. German, assistant professor of marketing.

Below: Employee members of our Management Development Board discuss Company operations with A&P officers.



Under another program to capitalize on our existing talent bank, we have begun holding "Career Days" in selected areas for A&P store personnel who may have an interest in pursuing long-term management and professional careers with our Company.

"Smart Moves," the theme of our new corporate-wide professional recruiting system, includes recruitment advertising, employment source cost control, direct sourcing and recruiting, internal staff selection, and staff planning and analysis.

A program to develop close, long-term relationships with the best college and technical schools has been established. Through direct recruitment and placement of students and graduates with the training and motivation for our business, A&P will be building a reservoir of managerial prospects on a permanent, co-op or part-time basis.

Internally, we have strengthened and expanded the responsibilities of our divisional directors of personnel. The addition of a number of experienced professionals in these posts has substantially raised the level of close support provided to our retail divisions.

Support for division managers and the division-level personnel management team comes from our group directors. The close relationship between these human resource specialists on the corporate level and operating management facilitates the determination of priorities, the implementation of new programs, and the most efficient application of A&P's total professional resources to the needs of the marketplace.

The entire A&P organization is represented to our customers, however, by the employees with whom they have direct contact. All of the resources of this corporation—all of its support systems—its purchasing power and its manufacturing capabilities—all of these converge during that critical period when a customer shops in one of our stores. The contact between that customer and our in-store professionals—the meat managers and butchers, the produce people, the deli department service staff—forms the foundation of customer attitude and loyalty.

And then comes that critical moment at the checkstand, "the last 18 inches"—in terms of our people and our front-end state of the art. Acknowledging the checkout counter as the hub of the store, we have provided our people with the finest, most advanced technology in the form of computerized, electronic point-of-sale equipment. Today, 425 units are on stream with ECR front ends, and two stores have gone operational with full scanning equipment.

The front-end not only is a funnel through which every item leaves the store and every dollar of sales is collected, but also a major source of store management information. The electronic point-of-sale checkout system allows for easy handling of complex checkout transactions and generates store operating reports on individual department sales, customer transactions, and hourly checker activity. Such data on the movement of selected items provide a gauge for developing more effective merchandising techniques. The feedback provided by this totally integrated system also aids in labor scheduling, loss prevention, cash control, and employee performance evaluation.

To capitalize on this important investment in electronic equipment, we have accelerated our training programs to sharpen technical and managerial skills and to develop the expertise of our key front-end people. Seventeen hundred supervisory and managerial people and several thousand cashiers have received and will continue to receive intensive training in those skills so critical to front-end operations.

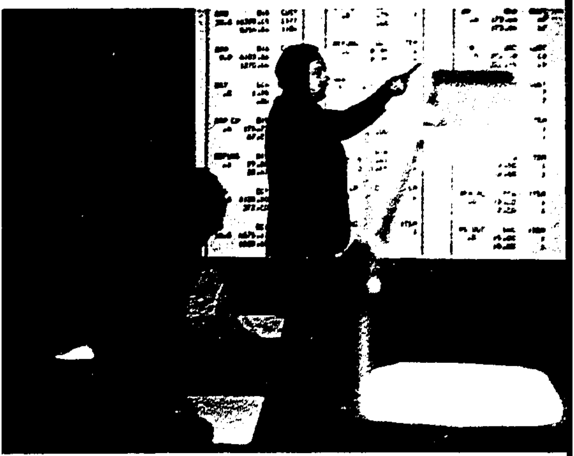
In the area of formalized training, the new A&P Institute at our Metro Region office in Paterson, New Jersey is providing a facility for fast-track personnel development. Equipped with the latest audio visual training aids, electronic front-end equipment, and a full complement of in-store equipment, the Institute program simulates a wide range of store operations and permits intensive training in a controlled workshop environment. The formalized Institute program is re-enforced by on-the-job instruction in selected stores, closely monitored and evaluated by training professionals. This pilot project is the forerunner of a network of Institutes we expect to establish throughout the Company.

As our number of training facilities grows, we will continue to reach out to all of our employees in stores, warehouses, manufacturing facilities, and offices via the medium of television. A&P's own Face-to-Face Communications Network produces video tapes for communicating with employees across a wide range of managerial, professional, and industry topics.

In Canada, we have undertaken an innovative "Creative Supervision" program, geared to developing and improving employee skills, a program which stresses interpersonal communications, motivation, employee value standards, performance evaluation, and coping with change. Based on the success of this program, we are now working toward adapting it for use in other other areas of A&P.

We are utilizing the services of local institutions of higher education and are also providing a self-teaching program. An independent home-study program with supervised follow-up examinations is giving new and experienced employees additional technical knowledge in store operations. Work simplification seminars for both supervisory personnel and plant employees are also producing tangible results.

Our new Train-the-Trainer program capitalizes on the skills of our experienced employees by enabling them to pass their knowledge along to other A&P people. As our management people accelerate their teaching role and join our formalized training force, more and more A&P people



will be brought to a higher level of efficiency and competency.

The foundations of an advanced management planning and development system were initiated in several areas, particularly within the Manufacturing Group. Innovative techniques in goal setting and performance measurement are being tested and are expected to provide models for application elsewhere within the Company.

As part of our advanced development system, the A&P Management Development Board, now in its fourth year of existence, provides selected administrative, executive, professional, and managerial employees the opportunity to study operations at first hand through face-to-face meetings with A&P officers, and contribute substantive recommendations for operating improvements. The Board is composed of 18 members, and each member serves for a period of 18 months. The purpose of this program is to accelerate the growth and development of talented employees who have the ability and motivation to become the future managers of A&P.

Center: Employees in the A&P store in Allendale, New Jersey, receive instruction in electronic scanner checkout.

Left top: Use of video cameras for in-store training allows instant monitoring of check-out performance.

Left bottom: A training session in progress at the A&P Institute in Paterson, New Jersey.

Below: Store manager Joseph Moran (right) and members of his store management team prepare to begin another day of "people to people" business.

Built into the Company's aggressive recruiting and career opportunities program is a commitment to A&P's Affirmative Action policies. An early participant in the Plans for Progress Program, A&P has reaffirmed and strengthened the commitment to social responsibility and pursued our goals through both recruiting and training programs.

Progress has been made in efforts to upgrade women and minorities despite the contraction of our work force. As an example, in 1975 minorities and women held few store manager or assistant manager positions. Today minorities hold 6.8% of our store manager positions and 4.0% of the assistant manager positions. Women hold 3.6% of our store manager positions and 1.5% of the assistant manager positions.

A&P's Industrial Relations structure and program also took a new, more flexible form in 1978. To meet the operating requirements of management and the cost pressures of a highly competitive marketplace while at the same time balancing the needs and expectations of employees, especially those covered by collective bargaining agreements, the Company initiated several significant changes.

Under a newly appointed director of research and planning, A&P has begun to develop its labor relations strategic planning over a longer time frame. Each individual market area will operate under an integrated plan which coordinates both long- and short-term objectives. These plans will be worked out in conjunction with operating management and with the Operations Planning Department, also established in 1978.

Our newly appointed Industrial Relations staff counsel provides close support legal assistance to the operating units and monitors all Equal Employment Opportunity proceedings to assure that A&P meets its responsibilities in this area.

A director of trust management was appointed to coordinate the activities of all A&P trustees sitting on Taft/Hartley Pension and Health Funds Boards to ensure that our employees receive the maximum benefit of the $50 million the Company contributes each year to the funds on their behalf.

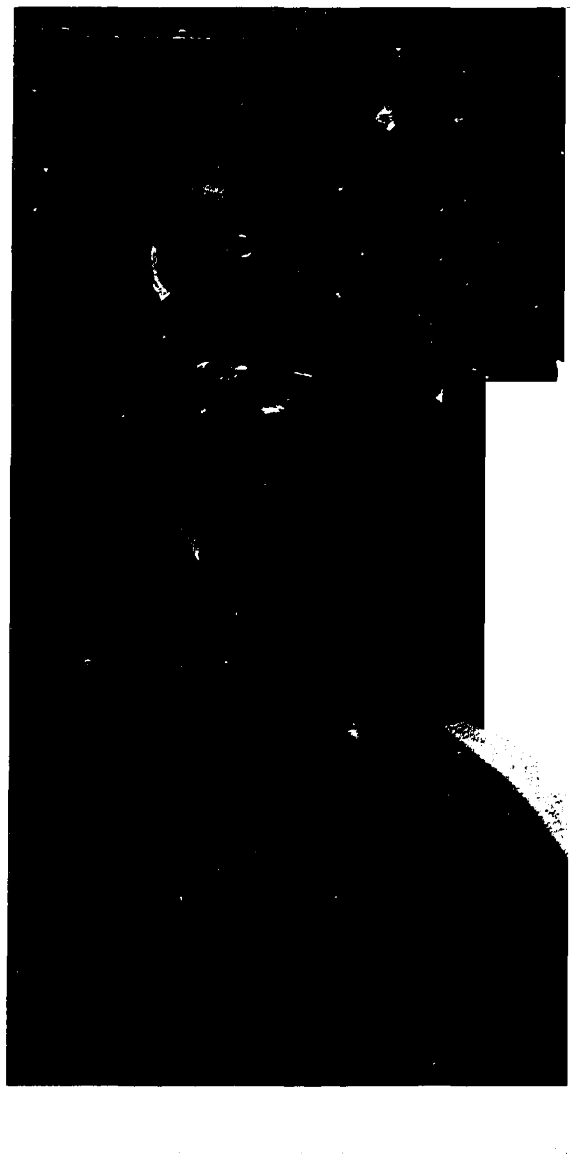
These organizational and operational changes are expected to significantly improve the Company's ability to meet the best interests of A&P, its employees, and its unions. This capability was demonstrated in 1978 when substantial improvements in A&P's competitive positions were achieved through the 31 new labor contracts negotiated during the year.

Major revisions have been made in A&P's Wage and Salary Program to achieve a better fit with today's realities in the marketplace for the best people. The program's objectives are to enable compensation costs to be more accurately budgeted and controlled, build on the principle of "pay for performance," and maintain a positive employee attitude and understanding that salary levels and progressions are equitably determined and provide a tangible incentive for high levels of performance.

A new Management Incentive Bonus Plan was instituted in 1978. Based on sales and profit performance, the plan is flexibly designed to reflect individual contribution from the corporate level to key field management positions. The "pay for performance" criterion is continued in this program.

Also in 1978, a broad re-evaluation was begun of all A&P benefit plans to assure currency, competitiveness, and cost effectiveness. The objective of the Company is to provide its employees the most appropriate and best quality benefit programs its means permit, and to assure that the maximum return on investment is achieved in terms of value to employees. Updating our total program will help to meet this objective.

In summary, A&P is engaged in one of the most intensive, advanced organization and personnel development programs in our industry. This con-



tinuing program benefits both employees at all levels of our Company, and A&P through the upgrading of its professional, managerial, and technical capability.

We believe that this "people investment" will, over the long term, contribute to our Company's productivity and help move us closer toward attaining sustained profitability.

Robert B. Runyon (standing at left), Executive Vice President, Human Resources, and William H. Watson (standing at center with side to camera), Vice President—Affirmative Action, and other A&P officials review progress of our Company's Affirmative Action programs with a team of consultants from OPT Associates.

Directors and Management Changes

Directors:
During the fiscal year Oscar L. Dunn, Jr., was elected to the Board of Directors, and Forwood C. Wiser Jr., resigned. Subsequent to year-end Edwin D. Dodd resigned, and Henry W. Van Baalen and Fritz Teelen were elected.

Corporate Officers:
During the year a number of senior management changes took place:

Robert B. Runyon was elected executive vice president—human resources.

Willis D. Lonn was promoted to executive vice president—merchandising and procurement.

Lawrence W. Snyder, previously a company officer, was elected a corporate officer with the title vice president—merchandising.

Gerald L. Good was elected vice president—operations planning.

Philip E. Hoversten, formerly assistant treasurer, was elected treasurer.

H. Nelson Lewis, previously a company officer, was elected a corporate officer with the title vice president—industrial relations.

Richard F. Doyle relinquished the title of treasurer and was named executive vice president, finance and chief financial officer.

Robert T. Blade, James L. Madden, and Robert L. Spencer, formerly corporate officers, were designated company officers as division vice presidents.

John J. Cairns, Jr., former vice president and region president; Roger L. Galassini, former vice president—administrative services; and Darrell V. Stiffler, Jr., former vice president—industrial administration resigned.

Financial Data

Auditors' Opinion

Deloitte Haskins & Sells
Certified Public Accountants

To the Board of Directors and Stockholders of The Great Atlantic & Pacific Tea Company, Inc.:

We have examined the consolidated balance sheets of The Great Atlantic & Pacific Tea Company, Inc. and subsidiary companies as of February 24, 1979 and February 25, 1978 and the related statements of consolidated operations, consolidated retained earnings (deficit) and changes in consolidated financial position for the fiscal years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, such financial statements present fairly the financial position of the companies as of February 24, 1979 and February 25, 1978 and the results of their operations and changes in their financial position for the fiscal years then ended, in conformity with generally accepted accounting principles applied on a consistent basis, after restatement for the change, with which we concur, in the method of accounting for leases as described under the caption Property in the Summary of Significant Accounting Policies and the caption Lease Obligations in the Financial Review which accompany the financial statements.

Deloitte Haskins & Sells

411 Hackensack Avenue
Hackensack, N. J. 07601
May 9, 1979

Fiscal Year—The Company's fiscal year ends on the last Saturday in February. Fiscal 1978 ended February 24, 1979 and Fiscal 1977 ended February 25, 1978.

Principles of Consolidation—The consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly-owned. All significant inter-company accounts and transactions have been eliminated.

Foreign Operations—Assets and liabilities of foreign subsidiaries have been translated at year end rates except for inventories, net property and certain deferred items which have been translated at historical rates. Income and expense accounts, except cost of merchandise sold and depreciation and amortization, have been translated at average rates prevailing during the fiscal year. Foreign exchange losses in fiscal 1978 amounted to $ 2.0 million compared with a loss of $2.4 million in fiscal 1977.

Inventories—Inventories are stated at the lower of cost or market, with cost being determined on the following bases: inventories in stores—average cost under the retail method; other inventories, primarily in warehouses and manufacturing facilities—cost on a first-in, first-out basis. Raw materials and supplies, principally at manufacturing facilities constituted approximately 7% and 10% of total inventories in fiscal 1978 and fiscal 1977, respectively.

Properties—The Company leases a substantial portion of its facilities. Leases, the majority of which are considered to be operating leases, are accounted for in accordance with Statement No. 13 of the Financial Accounting Standards Board (FASB No. 13). The accompanying financial statements for fiscal 1977 have been restated to reflect the retroactive application of FASB No. 13 which resulted in a decrease in earnings of $4,222,000, or $.17 per share. In addition, retained earnings as of February 27, 1977 was reduced by $17,030,000 representing the cumulative effect of this change on results of operations for fiscal years prior to 1977.

Owned land and buildings consist primarily of manufacturing facilities and warehouses. Equipment, store fixtures, and leasehold improvements generally are owned, although beginning in fiscal 1977 the Company has entered into equipment leasing programs for store equipment and trucks, most of which are accounted for as capital leases. Major additions and betterments are capitalized, whereas maintainence and repairs are charged to operations as incurred. When properties are replaced, retired, or otherwise disposed of, the cost of such properties and the accumulated depreciation are eliminated from the accounts in the year of sale or retirement. The gain or loss on the disposition of assets is recognized currently. Net losses on the disposition of closed facilities are charged to reserves previously provided therefor (see Closed Facilities accounting policy below).

Depreciation and Amortization—For financial reporting purposes, depreciation and amortization are provided, generally on the straight line method, over the estimated useful lives of the respective assets. Approximate annual depreciation rates for properties are as follows: buildings—2% to 5%; store and other equipment, except automotive— 8⅓% to 10%; store fixtures and leasehold improvements—10% to 12½% and automotive equipment—14²⁄₇% to 33⅓%. Equipment and real property leased under capital leases are amortized over the lives of the respective leases.

Pre-opening Costs—Costs incurred in the opening of a new store are expensed in the quarter in which the store is opened.

Closed Facilities—The Company provides for the estimated loss on the disposition of leased or owned facilities in the period in which the decision to close the facility is made. For significant closing programs, provisions are established for estimated closing costs including employee severance payments and other benefits, future operating losses of facilities to be closed and other related costs. The sales for those stores included in such significant closing programs are excluded from the statement of consolidated operations from the effective dates of inclusion in the programs.

Income Taxes—Deferred taxes have been provided in prior years in recognition of timing differences between income for financial reporting and income tax purposes. Approximately $7 million of deferred income taxes have not been provided on undistributed earnings of foreign subsidiaries considered to be permanently invested. Investment tax credits, previously utilized for tax purposes, have been deferred and are amortized over the estimated useful lives of the related assets.

Retirement Plans—Annual costs of the companies' pension plans, which are provided for currently, consist of normal cost, amortization over 40 years of unfunded prior service costs as of January 1, 1976, amortization over 30 years of changes in the unfunded actuarial liability resulting from plan amendments and changes in actuarial assumptions, and amortization over 15 years of annual actuarial gains or losses. Annual costs under union/management administered plans are expensed as provided for in the respective collective bargaining agreements.

Earnings Per Share—Net income (loss) per share is based on the weighted average number of common shares outstanding during the respective fiscal years. Stock options outstanding (common stock equivalents) had no material effect and, therefore, were excluded from the computation of net income (loss) per share.

Quarterly Information (unaudited)

The following table summarizes the Company's results of operations by quarter for fiscal 1978 and 1977. Management's Comments on the Summary of Operations, page 23, discusses these results and significant changes reflected therein.

	Quarterly Operating Results					Per Share Amounts				
	Number of Stores	Sales	Gross Margin	Income (Loss) before Extra-ordinary Item	Net Income (Loss)(c)	Income (Loss) before Extra-ordinary Item	Net Income (Loss)	Dividends	Market Price High	Market Price Low
Fiscal 1977 (a)		(millions)		(thousands)						
First Quarter	1,960	$1,780	$ 364	$ 3,101	$ 5,401	$ .12	$ .22	$—	$13⅛	$10
Second Quarter	1,931	1,827	382	171	271	.01	.01	.05	11½	9⅞
Third Quarter	1,917	1,811	393	(3,598)	(5,998)	(.14)	(.24)	.05	10½	7⅛
Fourth Quarter	1,905	1,871	412	895	895	.04	.04	.05	10¼	7¼
		$7,289	$1,551	$ 569	$ 569	$ .02	$ .02	$.15		
Fiscal 1978										
First Quarter	1,872	$1,808	$ 384	$ (9,919)	$ (9,919)	$ (.40)	$ (.40)	$.05	$ 9¼	$ 7⅝
Second Quarter	1,845	1,870	396	(6,883)	(6,883)	(.28)	(.28)	—	8	6¼
Third Quarter	1,801	1,884	412	1,506	1,506	.06	.06	—	7⅞	5
Fourth Quarter (b)	1,771	1,908	412	(36,890)	(36,890)	(1.48)	(1.48)	—	7¼	5⅛
		$7,470	$1,604	$(52,186)	$(52,186)	$(2.10)	$(2.10)	$.05		

(a) Restated in accordance with FASB No. 13.
(b) Results for the quarter include a net provision of $40 million representing the anticipated cost of the Restructuring Program. The number of stores at year-end includes stores to be closed in connection with the Restructuring Program (see Restructuring Program under Financial Review).
(c) Net income for the first and second quarters of fiscal 1977 includes charges in lieu of U.S. Federal income taxes, as well as equivalent amounts reflected as extraordinary credits in recognition of the corresponding tax benefit from the utilization of the Company's operating loss carryforward. Such amounts were reversed in the third quarter of fiscal 1977 as a result of the net loss incurred in that period.

Restructuring Program

On March 23, 1979, the Board of Directors approved a Restructuring Program which includes the closing of certain unprofitable and marginal stores and related support facilities. The program encompasses approximately 174 stores and certain manufacturing facilities, administrative offices, and a warehouse.

The foregoing restructuring of the Company's operations was based on a comprehensive analysis and study of the Company's organization undertaken during fiscal 1978 with the aid of a management consulting firm. A provision for the estimated cost of the Restructuring Program in the amount of $40 million, which represents a $51.7 million reserve, net of a reversal of deferred taxes totaling $11.7 million is included in the fiscal 1978 financial results.

The reserves for the anticipated cost of the Restructuring Program and the activity for fiscal 1978 and 1977 relative to reserves provided for a previous closing program, are summarized in the table below. Activity relating to reserves provided for closing of facilities under the Company's continuing program of evaluating all aspects of its operations are not shown therein.

(Dollars in millions)	Current Liabilities	Property Valuation	Non-Current Liabilities	Total
Balance February 26, 1977	$18.5	$3.0	$14.4	$35.9
Charges	(21.7)	(3.0)	—	(24.7)
Transfer to Current Liabilities	6.2	—	(6.2)	—
Balance February 25, 1978	3.0	—	8.2	11.2
Charges	(5.3)	—	—	(5.3)
Transfer to Current Liabilities	4.3	—	(4.3)	—
Anticipated Cost of Restructuring Program	33.8	8.3	9.6	51.7
Balance February 24, 1979	$35.8	$8.3	$13.5	$57.6

Stock Options

The Company has a stock option plan, approved by the Stockholders in June 1975, under which officers and key employees may be granted qualified or non-qualified options to purchase not more than 1,000,000 shares of common stock at not less than the fair market value at grant dates and for periods not exceeding ten years. In addition, options granted previously under a stock option plan approved by the Stockholders in 1969 were outstanding during fiscal 1977 and 1978; however, all remaining outstanding options granted under this plan lapsed in January 1979. A summary of option transactions is shown in the table below.

Of the non-qualified stock options outstanding at February 24, 1979, 240,000 were exercisable at the date of grant and as to the remaining 332,000 at cumulative 25% increments after each of the first through the fourth annual anniversaries of the grants. Qualified options are exercisable at cumulative 25% increments after each of the first through the fourth annual anniversaries of the grants, except for 10,000 options granted in fiscal 1978 which were exercisable at the date of grant. Proceeds from the exercise of stock options are credited to common stock for the aggregate par value of shares issued and the excess is credited to capital surplus, including $8,000 in fiscal 1977.

Summary of Option Transactions

	Shares		Option Price	
	Qualified	Non-Qualified	Per Share	Total
Outstanding, February 26, 1977	296,300	470,100	$ 9.25 to $12.56	$ 7,992,010
Fiscal 1977:				
Granted	—	75,000	7.81 to 12.06	859,525
Exercised	(960)	—	9.625	(9,240)
Cancelled or Expired	(45,040)	(35,000)	9.25 to 12.06	(848,960)
Outstanding, February 25, 1978	250,300	510,100	$ 7.81 to $12.56	$ 7,993,335
Fiscal 1978:				
Granted	15,000	105,000	5.88 to 8.19	812,430
Cancelled or Expired	(102,800)	(43,100)	7.81 to 12.25	(1,475,625)
Outstanding, February 24, 1979	162,500	572,000	$ 5.88 to $12.56	$ 7,330,140
Shares becoming exercisable in:				
Fiscal 1977	65,855	44,000	$ 9.625 to $12.56	$ 1,181,418
Fiscal 1978	46,875	56,750	$ 7.81 to $12.56	$ 1,114,603

264,600 options were available for future grant at February 24, 1979, while 202,500 were available at the end of the prior fiscal year.

Indebtedness

Long-term debt consists of:

	(Dollars in thousands)	
	February 24, 1979	February 25, 1978
9½% Senior Promissory Notes, due in 10 annual installments of $10,000,000 commencing October 1, 1983	**$100,000**	$100,000
9⅞% Mortgage Notes, due in monthly installments of $83,333 through September 29, 1997	**18,667**	19,667
Other Mortgage Notes, Interest rates of ⅞% to 9⅜%, due 1981 to 2002	**15,564**	16,188
	134,231	135,855
Less Current Maturities	**1,593**	1,628
	$132,638	$134,227

The agreements relating to the 9½% Senior Promissory Notes, among other things, prohibit the declaration of dividends until such time as net income subsequent to February 24,1979 (exclusive of the effect of the application of FASB No. 13 and as further defined in the agreements) exceeds approximately $38.5 million. Thereafter, aggregate dividends would be limited to 75% of net income as defined. The Company is also required to maintain consolidated working capital, as defined, of not less than $175 million. At February 24, 1979, consolidated working capital, as defined, was $220 million.

Maturities of long-term debt during each of the next five years are as follows:

1979	$ 1,593,000
1980	1,577,000
1981	1,577,000
1982	1,575,000
1983	11,607,000

The Company has established $73 million in lines of credit with commercial banks. During fiscal 1978, average daily bank borrowings under these agreements amounted to $11.3 million and the average daily interest rates for these borrowings were 7.7%. The maximum borrowings outstanding under these agreements at any month-end were $60 million in fiscal 1978.

In fiscal 1977, prior to the placement of the 9½% Senior Promissory Notes, the Company was borrowing under a 7½ year $50 million Term Loan and a $150 million Revolving Credit Agreement with a group of banks. The average daily borrowings under these agreements in fiscal 1977 were $61 million and the average daily interest rates for these borrowings were 7.6%. Maximum month-end borrowings under these agreements were $131 million. These agreements were cancelled concurrently with the placement of the 9½% Senior Promissory Notes. The average daily borrowings, average daily interest rates and the highest month-end amount outstanding under lines of credit with commercial banks during fiscal 1977 were $7 million, 7.6% and $35 million, respectively.

With respect to the lines of credit, and formerly the Revolving Credit Agreement, there are informal arrangements with the banks to maintain compensating balances, expressed in bank collected balances. The Company is expected, in some cases, to maintain average monthly bank collected balances totaling approximately 10 percent of the credit commitment plus 10 percent of outstanding loans made under the agreements. Such compensating balances requirements are not significant in relation to the Company's recorded cash balances.

Income Taxes

The provision for income taxes consists of the following:

(Dollars in thousands)	Fiscal 1978	Fiscal 1977
Relating to operations:		
Current:		
Canadian	$ 50	$ 140
State and Local	300	345
Amortization of Investment Tax Credits	(1,200)	(1,695)
	(850)	(1,210)
Deferred—Canadian	2,450	1,810
	$ 1,600	$ 600
Relating to Restructuring Program:		
Deferred—U. S.	$(11,669)	$ —

The anticipated cost of the Restructuring Program is deductible for income tax purposes in future years only as costs are actually incurred. The realization of the entire potential tax benefit of such costs is not considered assured beyond a reasonable doubt because of the Company's existing tax loss carryforward. Accordingly, only $11.7 million of the potential tax benefit, which is equivalent to previously provided net deferred U.S. income taxes that would become due during the tax loss carryforward period, is recognized for financial statement purposes.

The deferred Canadian provisions represent the excess of depreciation deductions of a Canadian subsidiary for tax purposes over amounts recorded for financial statement purposes.

At the end of fiscal 1978, the Company had an operating loss carryforward, for financial statement purposes of approximately $166 million which arose principally from provisions for closing of facilities. For tax purposes, the Company's operating loss carryforward is approximately $84 million which expires in fiscal 1982 through 1984. In addition, the Company has unused investment tax credits of approximately $28.4 million. These unused credits, which have not been recognized for financial statement purposes, will expire as follows: Fiscal 1981—$4.1 million, fiscal 1982—$6.7 million, fiscal 1983—$7.6 million, fiscal 1984—$7.1 million, and fiscal 1985—$2.9 million.

The difference between the Company's effective tax rate and the U.S. statutory tax rate is attributable to the Company's policy of amortizing investment tax credits, the effective rates of state and local income taxes, unrealized foreign exchange translation losses and, in fiscal 1978, to the $11.7 million deferred tax benefit discussed previously.

Retirement Plan

Retirement benefits for substantially all full-time and certain part-time employees are provided under the companies' retirement plans or by industry plans administered jointly by management and union representatives. The cost of all retirement plans amounted to $47.9 and $49.6 million in fiscal 1978 and 1977, respectively. During fiscal 1978, certain refinements relating to the actuarial assumptions utilized in the calculation of retirement plan costs were instituted; these refinements resulted in a reduction of pension costs to the Company of approximately $4 million for the year ended February 24, 1979. The companies' independent actuaries estimate that vested benefits under the companies' plans are fully funded at December 31, 1978. The Company could, under certain circumstances, be liable for substantial unfunded prior service or other costs of jointly administered union/management plans.

Litigation

In the 1974 Annual Report, the Company reported on an antitrust judgment entered in favor of a Mr. Bray and five other cattle producers or feeders in the amount of $35.8 million plus interest. The Company settled this action in 1975 (for payments over the next four years having a present value of about $7 million, which was charged to operations in fiscal 1975) and the judgment was vacated and the action dismissed.

During 1975 and 1976, nine similar antitrust suits, alleging violations of sections of the Sherman Act were filed in five states, and all of these were consolidated for pretrial purposes in the Dallas Federal Court. One of these actions was purportedly brought on behalf of a class consisting of all persons who are engaged in the business of raising fat cattle who have not otherwise filed claims and who sold more than 100 head of cattle per year. Each of these suits names the Company and other retail food chains as defendants and asks damages and other relief which may include an injunction. While most of these plaintiffs have not specified the amounts of damages they are claiming, their aggregate claims are substantial. In the actions in which money damages are specified or estimated, the plaintiffs allege damages exceeding $270 million.

On December 27, 1977, the District Judge hearing these actions entered a judgment dismissing all of them on the ground that plaintiffs had not sold directly to the retail food chain defendants, following Illinois Brick Co. v. the State of Illinois 431 US720 (1977). In all but one of such actions, the plaintiffs have appealed the judge's ruling. During 1977, seven additional antitrust suits alleging similar violations of the Sherman Act and seeking unspecified treble damages were filed in Texas and Utah. In certain of these new suits, meat packers to whom plaintiffs may have sold some of their cattle, are included as alleged co-conspirator defendants with the food chains. All these actions have been transferred to the Dallas Federal Court for pretrial purposes. A similar action has also been filed in California Superior Court but has been dismissed upon motion of the defendants and is presently on appeal.

In the above private actions, all of which are in the preliminary pretrial stages, money damages awarded to plaintiffs, if any, would automatically be trebled and such a judgment would also include reasonable plaintiffs' attorneys' fees.

As the result of the investigation of a charge filed on October 18, 1974 the Equal Employment Opportunity Commission ("Commission") issued a determination finding probable cause to support the allegation that the Company, several international unions and certain of their locals have violated the Civil Rights Act of 1964, as amended, by engaging in patterns and practices of employment discrimination. The Commission has submitted a proposed Consent Decree which would enjoin the defendants from the alleged discrimination in hiring, promotion and other employment practices, and require remedial measures, detailed implemental procedures and payments to alleged victims of discrimination.

The Company is also a defendant in an action filed on November 20, 1978 in the United States District Court for the Southern District of New York by Carmelo Maimone, his company and his associates, as a "Group... on behalf of itself and as the representative of a class of similarly situated shopping center owners and/or developers and/or builders". The Complaint alleges that defendants A&P and Booz Allen & Hamilton, Inc. agreed to reduce the number of A&P stores and discouraged developers from finding substitute tenants or from developing shopping centers for other tenants and that the Company breached its obligations to plaintiff. The Complaint alleges antitrust and other violations of law; it seeks treble damages in the amount of $90,000,000 and $300,000,000 in punitive damages, plus unspecified additional damages on behalf of the alleged class, as well as costs, attorneys' fees and other relief.

The Company denies all allegations of wrongdoing in the above mentioned actions. No provision for possible liability has been made in the accompanying financial statements.

The Company is also involved in various other claims, administrative agency proceedings and lawsuits arising out of the normal conduct of its business.

Although the ultimate outcome of the legal proceedings cannot be predicted, the Company's present opinion is that any resulting liability will not have a material effect upon the Company's financial position.

Lease Obligations

The Company operates primarily in leased facilities as it believes that its capital can be invested more productively in inventories and store equipment. Lease terms generally range up to twenty-five years for store leases and thirty years for other leased facilities, with options to renew for additional periods. The majority of the leases contain escalation clauses relating to property tax increases, and certain of the store leases provide for increases in rentals when sales at the stores exceed specified levels. In addition, the Company leases some store equipment and trucks because of financial and tax considerations. For stores leased under capital leases to be closed prior to lease expiration, the related assets and obligations are eliminated from the accounts as of the date of closing and an accrual is provided for anticipated costs to be incurred prior to the ultimate disposition of the facility.

The Company accounts for leases in accordance with FASB No. 13. Accordingly, the February 24, 1979 balance sheet includes $162,015,000 net of accumulated amortization of $60,133,000, for real property leased under capital leases and $37,608,000 net of accumulated amortization of $4,685,000, for equipment leased under capital leases. The February 25,1978 balance sheet, as restated, includes $177,419,000 net of accumulated amortization of $62,484,000, for real property leased under capital leases and $14,506,000 net of accumulated amortization of $984,000, for equipment leased under capital leases. The capitalized value of equipment leased under capital leases is included with owned equipment in the accompanying balance sheet.

Rent expense for operating leases aggregated $77,126,000 and $64,530,000 in fiscal 1978 and 1977 respectively, including $3,064,000 and $2,591,000 in contingent rentals. The minimum annual rentals for leases in effect at February 24,1979 are shown in the table below. All amounts are net of minor sublease rentals and exclusive of lease obligations applicable to closed facilities.

Minimum Annual Rentals

(Dollars in thousands)	Fiscal	Capital Leases Equipment	Capital Leases Real Property	Operating Leases
	1979	$ 7,430	$ 27,217	$ 60,009
	1980	7,430	27,104	55,445
	1981	7,430	26,787	49,533
	1982	7,430	26,139	45,104
	1983	7,430	25,500	42,213
	1984 and thereafter	14,760	278,273	337,434
		$51,910	$411,020	$589,738
Less executory costs		—	17,850	
Net minimum rentals		51,910	393,170	
Less interest portion		13,770	203,132	
Present value of net minimum rentals		$38,140	$190,038	

Replacement Cost (unaudited)

In response to the Securities and Exchange Commission requirements, the Company's Annual Report on Form 10-K, which is available on request, contains certain estimated replacement cost data regarding the costs of replacing inventories and productive capacity at February 24,1979 and February 25, 1978 and related information concerning depreciation and the cost of merchandise sold for the years then ended.

The replacement cost information disclosed in Form 10-K indicates that the cost of replacing the Company's productive capacity would be substantially higher than its original cost. The Company believes that, if this productive capacity were replaced, certain operating economies would result; however, these economies are not readily quantifiable. In addition, the estimated replacement costs reported do not necessarily indicate either the manner in which productive capacity would be replaced or the actual costs that would be incurred.

Statement of Consolidated Operations

(Dollars in thousands, except per share figures)	Fiscal 1978	Fiscal 1977
Sales	$7,469,659	$7,288,577
Cost of merchandise sold	5,865,637	5,738,002
Gross margin	1,604,022	1,550,575
Store operating, general and administrative expense	1,580,154	1,513,956
Income from operations	23,868	36,619
Anticipated cost of Restructuring Program	(51,669)	—
Interest expense:		
Capital leases	(23,420)	(22,639)
Other—net	(11,034)	(12,811)
Income (loss) before income taxes	(62,255)	1,169
(Provision) credit for income taxes relating to:		
Restructuring Program	11,669	—
Operations	(1,600)	(600)
Net income (loss)	$ (52,186)	$ 569
Per common share:		
Net income (loss)	$ (2.10)	$ .02
Dividends	$ .05	$ .15

Statement of Consolidated Retained Earnings (Deficit)

(Dollars in thousands)	Fiscal 1978	Fiscal 1977
Retained earnings—beginning of year	$ 49,135	$ 69,330
Cumulative effect of the capitalization of capital leases	—	(17,030)
Adjusted balance—beginning of year	49,135	52,300
Net income (loss)	(52,186)	569
Dividends	(1,245)	(3,734)
Retained earnings (deficit)—end of year	$ (4,296)	$ 49,135

See Financial Review and Summary of Significant Accounting Policies on Pages 13 through 19.

Consolidated Balance Sheet

Assets (Dollars in thousands)	February 24, 1979	February 25, 1978
Current assets:		
Cash and short-term investments	$ 94,716	$ 26,537
Accounts receivable	47,837	54,580
Inventories	544,525	592,357
Properties held for development and sale	25,790	44,311
Prepaid expenses	6,156	6,516
Total current assets	719,024	724,301
Property:		
Land	12,281	8,421
Buildings	77,721	72,727
Equipment	384,596	375,849
Total—at cost	474,598	456,997
Less accumulated depreciation	(193,889)	(186,629)
	280,709	270,368
Store fixtures and leasehold improvements, at amortized cost	113,856	121,530
	394,565	391,898
Less allowance for loss on property in facilities to be closed	(8,300)	—
	386,265	391,898
Real property leased under capital leases	162,015	177,419
Property—net	548,280	569,317
Other assets	13,922	12,349
	$1,281,226	$1,305,967

Liabilities and Stockholders' Equity (Dollars in thousands)	February 24, 1979	February 25, 1978
Current liabilities:		
Current portion of long-term debt	$ 1,593	$ 1,628
Current portion of obligations under capital leases	11,715	11,473
Accounts payable	265,022	301,645
Accrued salaries, wages and benefits	96,528	81,799
Accrued taxes, other than income taxes	41,055	39,463
Current portion of closing reserves and other accruals	95,308	46,475
Total current liabilities	511,221	482,483
Long-term debt	132,638	134,227
Obligations under capital leases	214,914	208,304
Deferred income taxes and investment tax credits	1,667	11,671
Closing reserves and other liabilities	22,891	17,956
Stockholders' equity:		
Preferred stock—no par value; authorized—3,000,000 shares; issued—none		
Common stock—$1 par value; authorized—40,000,000 shares; outstanding—24,892,084 shares	24,892	24,892
Capital surplus	377,299	377,299
Retained earnings (deficit)	(4,296)	49,135
Total stockholders' equity	397,895	451,326
	$1,281,226	$1,305,967

See Financial Review and Summary of Significant Accounting Policies on Pages 13 through 19.

Statement of Changes in Consolidated Financial Position

(Dollars in thousands)	Fiscal 1978	Fiscal 1977
Source of funds:		
From operations:		
Net income (loss)	$(52,186)	$ 569
Expenses (income) not requiring (providing) working capital:		
Depreciation and amortization	61,825	60,948
Amortization of real property leased under capital leases	12,607	12,130
Anticipated cost of Restructuring Program (non-current portion)	17,900	—
Deferred income taxes	(8,804)	1,810
Deferred investment tax credits	(1,200)	(1,695)
Working capital provided from operations	30,142	73,762
Disposition of property	19,781	1,442
Obligations under capital leases	34,980	17,722
Decrease in property leased under capital leases due to store closings, terminations, and amendments	23,297	4,973
Proceeds from borrowings	—	281,635
Total	108,200	379,534
Disposition of funds:		
Dividends	1,245	3,734
Expenditures for property	57,470	70,544
Property leased under capital leases	47,303	27,771
Decrease in obligations under capital leases due to store closings, terminations, and amendments	28.370	6,022
Current maturities and repayment of long-term debt	1,589	255,000
Transfer of non-current closing reserves to current liabilities	4,281	6,255
Other	1,957	2,436
Total	142,215	371,762
Increase (decrease) in working capital	(34,015)	7,772
Working capital—beginning of year	241,818	234,046
Working capital—end of year	$207,803	$241,818
Increase (decrease) in components of working capital:		
Cash and short-term investments	$ 68,179	$ 306
Accounts receivable	(6,743)	4,767
Inventories	(47,832)	25,346
Property held for development and sale	(18,521)	29,715
Prepaid expenses	(360)	(2,918)
	(5,277)	57,216
Accounts payable	(36,623)	29,096
Current portion of long-term debt	(35)	1,035
Current portion of obligations under capital leases	242	2,214
Income taxes payable	—	(1,423)
Accrued expenses	16,321	21,309
Current portion of closing reserves and other accruals	48,833	(2,787)
	28,738	49,444
Increase (decrease) in working capital	$(34,015)	$ 7,772

See Financial Review and Summary of Significant Accounting Policies on pages 13 through 19.

The following are management's comments on significant changes during the last five fiscal years. These comments should be read in conjunction with the Five Year Summary of Operations on page 24.

Fiscal 1978 Compared with Fiscal 1977
(as restated)

Sales for fiscal 1978 were $7.5 billion compared with $7.3 billion in fiscal 1977, a 2.5% increase. This increase was due primarily to inflationary increases, net of the impact of closing 186 stores (exclusive of the closings relative to the Restructuring Program), while opening 52 new stores. Average weekly sales per store increased $6,424, or 8.6% from $74,741 per store in the fourth quarter of fiscal 1977 to $81,165 in the same period of fiscal 1978.

Gross margin as a percent of sales increased from 21.3% in fiscal 1977 to 21.5% in fiscal 1978 due principally to continued improvements in product mix and a reduction in inventory losses.

Store operating, general and administrative expenses, as a percentage of sales, increased from 20.8% in fiscal 1977 to 21.2% in fiscal 1978 primarily due to increased labor and benefit costs, increased marketing and promotional costs, and higher rent and utility costs in new and enlarged stores offset, in part, by reductions in administrative costs.

During the fourth quarter of 1978, a $40 million reserve, net of a reversal of deferred taxes totaling $11.7 million was provided in connection with a Restructuring Program involving the closing of approximately 174 stores and certain manufacturing facilities, administrative offices, and a warehouse. The reserve includes amounts for the estimated losses to be incurred on the disposition of leased and owned properties, employee severance payments and other benefits, future operating losses of facilities to be closed, and other related closing costs.

Interest expense—other (net) decreased $1.8 million or 13.9% in fiscal 1978 as compared with fiscal 1977. This decrease was primarily due to reduced short-term borrowings in fiscal 1978 and increased income from short-term investments, resulting from improved cash management.

The net loss in fiscal 1978 aggregated $52.2 million, as compared with net income of $.6 million in fiscal 1977. The loss for fiscal 1978 was principally attributable to the anticipated cost of the Restructuring Program previously discussed, as well as the higher store selling, general and administrative expenses.

Included in the second quarter of 1978 is a charge of approximately $3.9 million, representing the estimated losses on stores and other facilities closed under the Company's continuing program of evaluating all aspects of its operations.

Fiscal 1977 includes a charge of $2.6 million in the third quarter for costs of closing a bakery and other related closing costs.

Both fiscal 1978 and 1977 reflect the capitalization of capital leases in accordance with Statement No. 13 of the Financial Accounting Standards Board; the charges to operations in fiscal 1978 and fiscal 1977 totaled $5.2 million and $4.2 million, respectively.

Fiscal 1977 Compared with Fiscal 1976
(as restated)

Sales for fiscal 1977 were $7.3 billion compared with $7.2 billion in fiscal 1976. This modest increase reflects the reduction in the number of stores in operation and the fact that sales of continuing stores in fiscal 1977 did not keep pace with inflation.

Gross margin as a percent of sales increased from 20.2% in fiscal 1976 to 21.3% in fiscal 1977 due to merchandising programs and improved product mix resulting, in part, from the larger average size of the new stores.

Store operating, general and administrative expenses were 20.8% of sales in fiscal 1977 as compared with 19.6% in fiscal 1976. This increase was due to higher labor and occupancy costs offset, in part, by reductions in administrative costs.

Interest expense—other (net) increased due to the higher level of borrowing in fiscal 1977.

Fiscal 1977 net income of $.6 million includes a $2.6 million provision for the closing of a bakery and other related closing costs. Fiscal 1976 net income of $18.7 million is after an extraordinary credit of $7.6 million representing the tax benefit of the Company's operating loss carryforward. Both fiscal 1977 and fiscal 1976 have been restated in accordance with Statement No. 13 of the Financial Accounting Standards Board, and include charges totaling $4.2 million and $5.0 million, respectively.

Significant Changes Prior to Fiscal 1976

Sales for the 52 weeks of fiscal 1976 were $7.2 billion compared with $6.5 billion in the 53 week period of 1975 and $6.9 billion in fiscal 1974. The increase in sales of 11% in fiscal 1976 was moderated by the effect of the 53rd week in fiscal 1975. The reduction in sales in fiscal 1975 as compared with fiscal 1974 was due to the closing of approximately 1,360 stores in that year.

Gross margins as a percent of sales were 19.5% and 19.8% for fiscal 1975 and 1974, respectively.

The net loss in fiscal 1974 was attributable to a $200 million provision for the closing of facilities, while the fiscal 1975 net loss of $32,000 included a $35 million reversal of the 1974 provision for the closing of facilities, representing the excess of estimated costs over actual costs incurred in the program.

Five-Year Summary of Operations

(Dollars in thousands, except per share figures)

For the Fiscal Year	1978	1977	1976	1975(c)	1974
Summary of Operations (e)					
Sales	**$7,469,659**	$7,288,577	$7,235,854	$6,537,897	$6,874,611
Cost of merchandise sold	**5,865,637**	5,738,002	5,770,698	5,260,844	5,514,580
Gross margin	**1,604,022**	1,550,575	1,465,156	1,277,053	1,360,031
Store operating, general and administrative expense	**1,580,154**	1,513,956	1,420,485	1,299,059	1,316,775
Income (loss) from operations	**23,868**	36,619	44,671	(22,006)	43,256
Provision for (adjustment of) cost of closing facilities	**51,669**	—	500	(35,000)	200,000
Interest expense:					
Capital leases	**23,420**	22,639	19,690	16,979	13,168
Other—net	**11,034**	12,811	5,294	4,447	1,701
Income (loss) before income taxes and extraordinary credit	**(62,255)**	1,169	19,187	(8,432)	(171,613)
Provision (credit) for income taxes	**(10,069)**	600	8,025	(6,600)	(11,200)
Income (loss) before extraordinary credit	**(52,186)**	569	11,162	(1,832)	(160,413)
Extraordinary credit	—	—	7,580	1,800	—
Net income (loss)	**(52,186)**	569	18,742	(32)	(160,413)
Depreciation and amortization (d)	**61,825**	60,948	54,590	53,709	51,620
Number of employees	**72,000**	81,000	90,000	92,900	105,000
Number of stores	**1,771**	1,905	1,978	2,074	3,468
Total store-area (square feet)	**36,935,000**	38,354,000	38,478,000	39,202,000	55,763,000
Balance Sheet Data (e)					
Total assets	**1,281,226**	1,305,967	1,227,197	1,147,470	1,154,258
Working capital	**207,803**	241,818	234,046	235,868	207,365
Current ratio	**1.41**	1.50	1.54	1.58	1.44
Additions to property (d)	**84,273**	104,814	94,763	65,880	80,363
Property-net	**548,280**	569,317	550,562	497,367	474,439
Long-term debt	**132,638**	134,227	107,592	78,520	39,075
Stockholders' equity	**397,895**	451,326	454,482	435,623	435,632
Common Stock Data (e)					
Income (loss) per share before extraordinary credit (a)	**(2.10)**	.02	.45	(.07)	(6.45)
Extraordinary credit per share (a)	—	—	.30	.07	—
Net income (loss) per share (a)	**(2.10)**	.02	.75	—	(6.45)
Cash dividends per share	**.05**	.15	—	—	.45
Stockholders' equity per share (b)	**15.98**	18.13	18.26	17.12	17.51
Shares outstanding (a)	**24,892,084**	24,892,084	24,885,630	24,878,012	24,876,644
Number of stockholders	**36,556**	38,012	40,200	40,900	42,100

(a) Based on the weighted average number of common shares outstanding each year.
(b) Based on the number of common shares outstanding at each year-end.
(c) 53 weeks; all other years contained 52 weeks.
(d) Excludes real property leased under capital leases, and includes equipment leased under capital leases.
(e) Fiscal years 1974 through 1977 have been restated to reflect the impact of the application of FASB No. 13.

Directors

William M. Agee
Chairman and
Chief Executive Officer
The Bendix Corporation

Harold J. Berry
Chairman, Investment
Banking Committee
Merrill Lynch, Pierce,
Fenner & Smith Inc.

Walter D. Dance
Vice Chairman of the Board
and Executive Officer
General Electric Company

Charles F. Detmar, Jr.
Partner,
Cahill Gordon & Reindel
Attorneys

Oscar L. Dunn, Jr.
Chairman of the Board of
Directors and Chief
Executive Officer
New York Chamber of
Commerce and Industry

Allan A. Feder
Executive Vice President,
President—
Manufacturing Group

Barbara Barnes Hauptfuhrer

David W. Morrow
President and Chief
Operating Officer

Jonathan L. Scott
Chairman of the Board
of Directors and Chief
Executive Officer

Hobart Taylor, Jr.
Partner,
Dawson, Riddell, Taylor,
Davis & Holroyd
Attorneys

Fritz Teelen
Vice President,
Plus Warenhandelsgesell-
schaft mbH & Co.OHG
West Germany

Edward J. Toner
Partner,
Collins, Toner & Rusen
Attorneys

Henry W. Van Baalen
Consultant
Tengelmann Group
West Germany

Corporate Officers

Jonathan L. Scott
Chairman of the Board of
Directors and Chief
Executive Officer

David W. Morrow
President and Chief
Operating Officer

Richard F. Doyle
Executive Vice President,
Finance and Chief
Financial Officer

Allan A. Feder
Executive Vice President,
President—
Manufacturing Group

Willis D. Lonn
Executive Vice President,
Merchandising and
Procurement

John J. Miles
Executive Vice President

Lowell A. Peters
Executive Vice President

Robert B. Runyon
Executive Vice President,
Human Resources

William I. Walsh
Executive Vice President

John L. Dean
Vice President—
Management Information
Services

Ivor D. Donaldson
Vice President—
Property Development

Gerald L. Good
Vice President—
Operations Planning

James T. Gow, Jr.
Vice President—
Warehousing and
Distribution

Philip E. Hoversten
Treasurer

H. Nelson Lewis
Vice President—
Industrial Relations

Arthur C. Mclervey
Secretary

Earl N. Pilgrim
Vice President—
Purchasing

Robert M. Quinn
Controller

Louis A. Savarese
Vice President—
Production

Lawrence W. Snyder
Vice President—
Merchandising

Robert G. Ulrich
Vice President and
General Counsel

Harold N. Tolchinsky
Assistant Secretary

Executive Offices
Box 418
2 Paragon Drive
Montvale, New Jersey
07645
Telephone 201-573-9700

Transfer Agent and Registrar
Morgan Guaranty Trust
Company of New York
New York, N.Y.

Common stock of the Company is traded on the New York Stock Exchange under the symbol "GAP," and has unlisted trading privileges on the Boston, Midwest, Philadelphia—Baltimore-Washington, Pittsburgh, Cincinnati and Detroit Stock Exchanges.

The Annual Meeting will be held on Friday, July 6, 1979, at 10 a.m. at the Radisson Plaza Hotel, Two NCNB Plaza in Charlotte, North Carolina. Stockholders are cordially invited to attend.

Copies of the Form 10-K submitted to the Securities and Exchange Commission will be provided to stockholders upon written request to the Secretary.

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